

**OFFICIAL FILE**

ILL. C. C. DOCKET NO. 04-0299

*NCC Staff* EXHIBIT NO. 1.0 *Revised*

Witness \_\_\_\_\_

Date 5-14-04 Reporter *and*

**DIRECT TESTIMONY**

**OF**

**MARK A. HANSON**

**TELECOMMUNICATIONS DIVISION**

**ILLINOIS COMMERCE COMMISSION**

**FAIRPOINT COMMUNICATIONS INC., C-R TELEPHONE COMPANY, THE EL  
PASO TELEPHONE COMPANY, ODIN TELEPHONE EXCHANGE, INC. AND  
YATES CITY TELEPHONE COMPANY**

**JOINT APPLICATION FOR APPROVAL OF THE RECAPITALIZATION OF  
FAIRPOINT COMMUNICATIONS INC. PURSUANT TO SECTIONS 7-203 AND  
7-204 AND FOR OTHER RELIEF.**

**DOCKET NO. 04-0299**

**MAY 7, 2004**

1  
2 **Q. State your name and business address.**

3 A. My name is Mark A. Hanson. My business address is 527 East Capitol,  
4 Springfield, Illinois 62701.  
5

6 **Q. By whom are you employed and in what capacity?**

7 A. I am employed by the Illinois Commerce Commission as a Rate Analyst in the  
8 Telecommunications Division.  
9

10 **Q. Please describe your education and occupational background.**

11 A. I received a Bachelor of Science degree in Commercial Economics from South  
12 Dakota State University in 1978. I received a Master of Science degree in  
13 Economics from South Dakota State University in 1981. From 1981 to 1987, I  
14 was employed by the South Dakota Department of Transportation as a  
15 Transportation Planner. From 1987 to 1989, I was enrolled in the doctoral  
16 program in Economics at Iowa State University. While at Iowa State, I was  
17 employed as an instructor in the Agricultural Business department and also as  
18 an instructor in the Transportation/Logistics department. From 1990 to 2000, I  
19 was employed by Illinois Power Company as a Forecast Specialist, Regulatory  
20 Matters Specialist, Gas Supply Specialist, and Competitive Pricing Specialist. I  
21 joined the Staff of the Commission in July 2000.  
22

23 **Q. Briefly describe your duties with the Illinois Commerce Commission.**

24 A. My responsibilities include reviewing wholesale and retail tariff filings for both  
25 competitive and non-competitive telecommunications services, providing  
26 support to other Commission Staff, and analyzing cost study issues in  
27 docketed cases that have cost of service and rate implications. I am also  
28 responsible for reviewing the managerial, technical, and financial capabilities  
29 of companies seeking approval to do business in Illinois as competitive local  
30 exchange carriers.

31

32 **Q. Have you previously testified before any regulatory agencies?**

33 A. I have testified before this Commission in several different proceedings  
34 concerning telecommunications matters. Those proceedings include Docket  
35 Nos. 98-0252/98-0335 (Consol.), Docket No. 00-0641, Docket Nos. 00-  
36 0511/00-0512(Consol), Docket No. 01-0279, Docket No. 01-0515, Docket No.  
37 00-0812, Docket No. 01-0662, Docket No. 02-0365, Docket No. 02-0864,  
38 Docket No. 03-0239, Docket No. 03-0593, Docket No. 03-0596, and Docket  
39 No. 03-0779. I have also testified before the Federal Energy Regulatory  
40 Commission.

41

42 **Q. What is the purpose of your testimony?**

43 A. In this proceeding, FairPoint Communications, Inc. ("FairPoint"), C-R  
44 Telephone Company, The El Paso Telephone Company, Odin Telephone  
45 Exchange, Inc. and Yates City Telephone Company (collectively referred to as  
46 "Operating Companies") are petitioning the Commission for permission to

47 implement a recapitalization plan. The Commission must determine that the  
48 companies meet the requirements of Sections 7-203 and 7-204 of the Public  
49 Utilities Act ("PUA") or ("the Act") in order to proceed with the recapitalization  
50 plan. Based upon my review of the Joint Application filed by FairPoint and the  
51 Operating Companies, I suggest a couple of conditions regarding cost and rate  
52 issues that the Commission should order FairPoint and the Operating  
53 Companies to comply with prior to approving the requested recapitalization  
54 pursuant to Sections 7-203 and 7-204 of the Act. Staff witness Janis Freetly  
55 (Staff Exhibit 2.0), of the Commission's Finance Department, will offer  
56 testimony on FairPoint's and the Operating Companies' compliance with  
57 financial standards and suggest a couple of conditions the Commission should  
58 impose upon the companies before the recapitalization is approved. Theresa  
59 Ebrey (Staff Exhibit 3.0), of the Commission's Accounting Department, will offer  
60 comments on FairPoint's and the Operating Companies' compliance with the  
61 requirements of Sections 7-203 and 7-204 with respect to subsidization issues.  
62 Finally, Samuel S. McClerren (Staff Exhibit 4.0), of the Engineering Department  
63 of the Telecommunications Division, will suggest a set of service quality  
64 conditions to ensure that customers of Illinois utilities do not suffer declines in  
65 service quality as a result of this recapitalization.

66  
67 **Q. What are Fairpoint's obligations under Section 7-204 of the Public**  
68 **Utilities Act with respect to rate and cost issues?**

69 **A.** Section 7-204(b)(7) requires a petitioner to show that "the proposed

reorganization is not likely to result in any adverse rate impacts on retail customers.” Section 7-204(c) requires that “the Commission shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed reorganization; and (ii) whether the companies should be allowed to recover any costs incurred in accomplishing the proposed reorganization and, if so, the amount of costs eligible for recovery and how the costs will be allocated.”

**Q. Will this reorganization have adverse rate impacts upon retail customers?**

A. Mr. Leach states in his direct testimony that Fairpoint and its Operating Companies will not likely have any adverse rate impacts upon its retail customers.<sup>1</sup> To ensure that no adverse rate impacts occur as a result of the recapitalization to the customers of C-R Telephone Company, The El Paso Telephone Company, Odin Telephone Exchange, Inc. and Yates City, I recommend that the Commission impose a condition upon FairPoint’s Operating Companies.

**Q. Please explain the condition you propose.**

A. I propose that C-R Telephone Company, The El Paso Telephone Company, Odin Telephone Exchange, Inc. and Yates City be prohibited from increasing tariffed retail rates for one year after the effective date of the reorganization. Additionally, the Operating Companies should not be allowed to use any increased costs, as a result of this recapitalization, to justify any increases in

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<sup>1</sup> FairPoint Exhibit 1.0 at 18

their levels of support from the Universal Service Fund.

**Q. Has the Commission previously imposed similar conditions to ensure that the requirements of Section 7-204(b) (7) are met?**

A. Yes. In Docket No. 00-0161, the Commission imposed a condition upon MJD Communications, Inc., to not increase retail rates as a result of a recapitalization. I note that it appears that MJD Communications Inc. was FairPoint's previous name, since the Docket 00-0161 Order identifies MJD Communications, Inc., like FairPoint, as being the holding company that owned and controlled the Operating Companies involved in this joint application.

**Q. What is the level of savings resulting from the reorganization and how should the Commission allocate those savings?**

A. According to Mr. Leach, there are no savings from the reorganization and thus there are no allocation issues. Since this reorganization is principally a financial transaction with no operational savings, that appears to be a reasonable statement. I believe there is no issue to be resolved with respect to Section 7-204(c).

**Q. Besides cost and rate issues, are there other parts of Section 7-204(b) that you will address?**

A. Yes. I will address Section 7-204(b)(1), Section 7-204(b)(5), and Section 7-204(b)(7).

115

116 **Q. What are the requirements of Section 7-204(b)(5)?**

117 A. This requirement states, "the utility will remain subject to all applicable laws,  
118 regulations, rules, decisions, and policies governing the regulation of Illinois  
119 public utilities."

120

121 **Q. Did FairPoint's witness make any statements regarding the intent of the**  
122 **Companies with respect to this code part?**

123 A. Yes. Mr. Leach specifically acknowledged that FairPoint and each of the  
124 Operating Companies will remain subject to all applicable laws, regulations,  
125 rules, decisions, and policies governing the regulation of Illinois incumbent local  
126 carriers.<sup>2</sup>

127

128 **Q. What are the requirements of Section 7-204(b)(7) ?**

129 A. This requirement states, "the proposed reorganization is not likely to have a  
130 significant adverse effect on competition in the markets over which the  
131 Commission has jurisdiction."

132

133 **Q. In your opinion, will this reorganization have a significant adverse impact**  
134 **on competition in markets over which the Commission has jurisdiction?**

135 A. No. This reorganization is primarily financial in nature. Allowing it to proceed  
136 should have no impact on competition in the markets in which these companies

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<sup>2</sup> Fairpoint Exhibit 1.0 at 17

137 operate.

138

139 **Q. What are the requirements of Section 7-204(b)(1)?**

140 A. This requirement states, "the proposed reorganization will not diminish the  
141 utility's ability to provide adequate, reliable, efficient, safe, and least cost utility  
142 service."

143

144 **Q. In your opinion, will this reorganization meet the requirements of Section**  
145 **7-204(b)(1)?**

146 A. In addition to my suggested conditions, Staff witnesses Freetly, Ebrey, and  
147 McClerren suggest various conditions. Adopting these conditions as part of  
148 approving the reorganization will ensure that this reorganization meets the  
149 requirements of Section 7-204(b)(1).

150

151 **Q. Will you summarize the conditions Staff recommends the Commission**  
152 **impose upon FairPoint and the Operating Companies?**

153 A. Staff proposes that the following conditions be imposed in connection with the  
154 transaction:

155 1) Staff should be granted access to all books, accounts, records, and  
156 personnel of FairPoint Communications Inc., C-R Telephone Company, The  
157 El Paso Telephone Company, Odin Telephone Exchange, Inc. and Yates  
158 City Telephone Co. and all of their utility and non-utility affiliated parent,



- 159 sister and subsidiary companies, as well as independent auditors' work  
160 papers. See Theresa Ebrey's Testimony, Exhibit 3.0;
- 161 2) C-R Telephone Company, The El Paso Telephone Company, Odin  
162 Telephone Exchange, Inc. and Yates City Telephone Co. should continue  
163 to comply with 83 Ill. Adm. Code 712. See Theresa Ebrey's Testimony,  
164 Exhibit 3.0;
- 165 3) FairPoint Communications Inc., C-R Telephone Company, The El Paso  
166 Telephone Company, Odin Telephone Exchange, Inc. and Yates City  
167 Telephone Co. and all of their utility and non-utility affiliated parent, sister  
168 and subsidiary companies should conduct annual internal audits to test  
169 compliance with Sections 7-204(b)(2) and 7-204(b)(3). The internal audit  
170 report documenting findings, conclusions, and recommendations should be  
171 submitted to the Manager of Accounting of the Illinois Commerce  
172 Commission by March 31<sup>st</sup> each year and associated work papers should  
173 be available to Commission Staff for review. The first internal audit report  
174 shall be submitted to the Manager of Accounting of the Commission on or  
175 before March 31, 2005. See Theresa Ebrey's Testimony, Exhibit 3.0;
- 176 4) that C-R Telephone Company, The El Paso Telephone Company, Odin  
177 Telephone Exchange, Inc. and Yates City Telephone Co. be prohibited from  
178 increasing tariffed retail rates for one year after the effective date of the  
179 reorganization. See above;
- 180 5) the C-R Telephone Company, The El Paso Telephone Company, Odin

Telephone Exchange, Inc. and Yates City Telephone Co. are prohibited from using any increased costs, as a result of this recapitalization, to justify any increases in their levels of support from the Universal Service Fund. See above;

6) an Operating Company (i.e. C-R Telephone Company, The El Paso Telephone Company, Odin Telephone Exchange, Inc. and Yates City Telephone Co.) will be prohibited from paying dividends to FairPoint Communications Inc. or from otherwise transferring cash to FairPoint Communications Inc. through loans, advances, investments or other means that would divert their moneys, property or other resources that is not essentially or directly connected with the provision of non-competitive telecommunications service if that operating company fails to meet or exceed the standard, set herein, for a majority of the service quality measures. See Janis Freetly's Testimony, Exhibit 2.0;

a) STANDARDS: Standards shall be developed for each operating company's performance with respect to each service quality measure. If any of the Operating Company's are granted a permanent waiver from having to comply with a key service quality measure, then that service quality measure shall not be included in the list. Until the Commission issues an order in Dockets 04-0278 through 04-0281, key service quality measures 730.510(a)(1)(A), 730.510(a)(1)(B), 730.510(b)(1), and 730.510(b)(1) shall be included in the condition, but not used to determine compliance with this condition. If a permanent

waiver is denied, then those service quality measures shall be used to determine compliance. A standard shall be the average of the two year actual performance of that operating company for that service quality measure, for the past twenty-four months. See Samuel S. McClerren's Testimony, Exhibit 4.0;

b) MEASUREMENTS: Measurements shall commence on the date the securities are issued, and will be taken on an annual basis. The service quality measures subject to this condition are:

730.510(a)(1)(A) - Toll & Assistance Answer Time

730.510(a)(1)(B) - Information Answer Time

730.510(b)(1) - Business Office Answer Time

730.510(b)(1) - Repair Office Answer Time

730.535(a) - Interruptions of Service

730.540(a) - Installation Requests

730.545(a) - Trouble Reports

See Samuel S. McClerren's Testimony, Exhibit 4.0;

c) ANNUAL REPORTS: FairPoint Communications Inc. shall file an annual report with the Chief Clerk's Office and posted in this docket. The annual report shall be filed December 1 of each year. Within the annual report, FairPoint Communications Inc. shall identify each carrier, and the title of the service quality measure, and by operating company FairPoint Communications Inc. shall list the standard set by the

Commission for each service quality measure, and the actual performance for each annual period. The annual report shall present the actual performance data for every month after the date the securities are issued, with the initial month of data presented in the report being July 2004. See Samuel S. McClerren's Testimony, Exhibit 4.0;

d) FINAL NOTICE: When FairPoint Communications Inc.'s issuer credit rating from both Standard & Poor's and Moody's Investors Service improves to investment grade, FairPoint Communications Inc. shall send a certified notice to the Commission, with a third-party independent verification that its issuer credit rating has been upgraded to investment grade. A corporate officer shall certify that the notice is true and accurate. See Janis Freetly's Testimony, Exhibit 2.0;

e) DURATION OF CONDITON: The duration of time this condition should remain in effect is until FairPoint Communications Inc.'s issuer credit rating increases to investment grade. See Janis Freetly's Testimony, Exhibit 2.0;

7) that FairPoint keep available exclusively for the Illinois operating telephone companies, under its senior secured credit facility, an amount equal to the higher of \$1 million or the currently approved capital expenditures budget

250 for all four Illinois operating telephone companies. FairPoint should certify  
251 annually to the Commission that the required amount is available to the  
252 Illinois operating companies for the ensuing year. Therefore, on December  
253 1 of each year, FairPoint shall send a notice to the Commission  
254 certifying that such amount was then currently available, and for the  
255 ensuing year what the dollar commitment would be for the Illinois  
256 companies based on the capital expenditure budget for the following year.  
257 See Janis Freetly's Testimony, Exhibit 2.0.

258

259 **Q. Does this conclude your direct testimony?**

260 A. Yes, it does.

261